

Nike Flyknit may reinvent iconic swoosh

Premium content from Portland Business Journal by Erik Siemers , Business Journal staff writer

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Nike Inc. CEO Mark Parker believes the manufacturing technology behind the company's Flyknit Racer shoes will help improve the company's profit margins as it spreads to other products.

When [Nike Inc.](#) unveiled its new Flyknit shoe technology, it was hailed for doing all of the things Nike shoes are supposed to do.

The Flyknit Racer running shoe is lightweight, performance enhancing, sustainable and innovative — all pillars of the Nike brand.

But last week Nike executives were praising Flyknit for another feature: The ability to expand profit margins.

Nike CEO [Mark Parker](#) believes Flyknit can be applied across all of Nike's footwear categories, and even apparel, depicting Flyknit as almost the perfect product on all fronts.

"There's the leverage we get from a production standpoint, the sustainability story and then, of course, performance," Parker told analysts on a conference call last week. "We do see this as a way not only to create a higher performance, more sustainable product but one that actually will gives us significantly better margins as we scale this."

Traditionally, shoes are made out of various types of material cut and stitched together, a somewhat labor intensive process that produces significant material waste.

With Flyknit, Nike has engineered a system using a specialized yarn knit together into a one-piece, sock-like upper, which covers the toes and top of the foot.

The process is also highly automated, reducing labor costs. Though Nike hasn't released exact cost savings data from the manufacturing process, the company says the Flyknit Racer running shoe creates two-thirds less waste than typical running shoes.

The new production technique comes as Nike — and the footwear industry as a whole — feels the weight of increased costs impinging on profit margins.

Nike sales gained 15 percent in its fiscal 2012 third quarter, reaching \$5.8 billion and easily beating Wall Street expectations.

But its gross margin fell by 2 percent to 43.8 percent, sending its shares tumbling downward. Nike stock reached nearly \$112 in after-hours trading after its results were announced last Thursday. By Wednesday, it was trading at \$107, a nearly 5 percent drop.

common problem

Nike isn't alone in battling higher costs.

The amount of footwear imported into the U.S. last year fell 3.4 percent, but the higher costs to make those products sent import prices for footwear up 12.2 percent, according to a report released earlier this month by the Footwear Distributors and Retailers of America.

"This demonstrates what has been painfully obvious to the industry for some time — we are facing inflation in the midst of a sluggish economic environment," the report states.

Footwear brands like Nike and Washington County neighbor Columbia Sportswear Co. have responded to higher input costs by raising prices at the retail level.

Year to date, the average price for men's sneakers has risen 4.4 percent to \$69.21, according to Matt Powell, an analyst with industry research firm SportsOne Source.

So far, higher prices haven't impaired retail sales, but Parker said Nike isn't "sitting around and waiting for prices on materials" to drop.

"We're acting very aggressively to apply any opportunity we think is meaningful to really innovate in other ways to take those input costs down and ... to improve our gross margin picture," he said.

Flyknit is one such innovation.

“You’re looking at a shoe that is probably 93 to 96 percent no waste,” said [Brett Golliff](#), a footwear blogger who spent four years designing shoes at Boston-based [New Balance Athletic Shoe Inc.](#) “That’s huge. Especially if they can spin a performance story on it. Traditionally you get something eco-friendly, there was never a shoe that could perform.”

The ease of production also raises the possibility of localizing manufacturing, thereby eliminating expensive shipping costs.

Golliff penned an essay on the site CounterKicks.com last week in which he forecast a time five years from now when consumers could walk into a Nike store, choose from a selection of mid-soles and thread types to create a completely customized shoe built, potentially, on site.

He compared it to buying groceries at Whole Foods. The material is sourced locally and sold at a premium price.

“It’s already built for you, and that much easier to produce,” Golliff said. “Their revenue is going to be ridiculous.”

But the concept isn’t without its challenges.

[D’Wayne Edwards](#), the former head designer at Nike’s Jordan Brand who now runs the footwear design program Pensole in downtown Portland, believes Nike’s next big challenge is applying Flyknit to sports other than running.

Edwards said the Flyknit design, for now, appears limited to linear sports — activities where the athlete moves forward, but not left and right.

To be useful in basketball and tennis — sports that require significant lateral movement — it needs to have a backing that provides stability to the forefoot, or a new configuration that takes advantage of the strength of woven material.

“Right now you get the ease of manufacturing opportunity,” Edwards said. “But when you get into making it work for other activities, then it becomes a performance enhancement opportunity.”

In Parker’s viewpoint, that opportunity for Nike and its profit margins is boundless.

“Flyknit has the potential to change everything,” Parker said. “We’re at the very front end of the potential here.”